Auditor-General of South Africa

eDumbe Municipality - Audit report 2014-15

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the Council on eDumbe Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the eDumbe Municipality set out on pages … to …, which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2014 (Act No. 10 of 2014) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on the financial statements based on my audit. I conducted my audit in accordance with International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the eDumbe Municipality as at 30 June 2015 and its financial performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

I draw attention to the matters below. My opinion is not modified in respect of these matters.

Significant uncertainties

7. As disclosed in note 46 to the financial statements, the municipality is the defendant in a number of lawsuits related to contracts entered into by the municipality. The municipality is opposing some of the claims, as it believes the claims to be fraudulent or unwarranted. The ultimate outcome of these matters cannot presently be determined.

Material losses and impairments

8. As disclosed in note 44 to the financial statements, material electricity losses amounting to R4,70 million (2014: R6,4 million), were incurred as a result of technical and non-technical distribution losses.
9. As disclosed in note 7 to the financial statements, the municipality provided for impairment on property, plant and equipment amounting to R1,53 million (2014: R19 150) due to conditional assessments that were performed.
10. As disclosed in note 5 to the financial statements, the municipality provided for impairment of receivables from exchange transactions amounting to R6,60 million (2014: R8,39 million) due to poor collection practices.

Going concern

11. As disclosed in note 47 to the financial statements, the municipality was not able to pay instalments on a DBSA loan, conditional grants were not backed by cash and the liquidity ratio was unfavourable resulting in an inability to pay creditors timeously. These conditions, along with other matters stated in the abovementioned note indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern in the foreseeable future.

Additional matters

12. I draw attention to the matters below.

Unaudited supplementary schedules

13. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules, and accordingly, I do not express an opinion thereon.

Report on other legal and regulatory requirements

14. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

15. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for basic service delivery and infrastructure development as well as good governance and public participation development priorities presented in the annual performance report of the municipality for the year ended 30 June 2015.

16. I evaluated the reported performance information against the overall criteria of usefulness and reliability.

17. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).

18. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

19. The material findings in respect of the selected development priorities are as follows:

Basic service delivery and infrastructure development

Usefulness of reported performance information

Measurability of indicators and targets

Performance targets not specific and measurable and indicators not well defined

20. Performance targets should be specific in clearly identifying the nature and required level of performance as required by the FMPPI. A total of 30,7% of the targets were not specific.

21. Performance targets should be measurable as required by the FMPPI. I could not measure the required performance for 30,7% of the targets.

22. Performance indicators should be well-defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. A total of 23% of the indicators were not well-defined.

23. This was due to a lack of proper systems and processes and/or technical indicator descriptions.

Reliability of reported performance information

24. The FMPPI requires municipality's to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. Overall, 25,3% of the targets were not reliable because I was unable to obtain sufficient appropriate audit evidence for significantly important targets.

Good Governance and Public Participation

Reliability of reported performance information

25. The FMPPI requires municipality's to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. Adequate and reliable corroborating evidence could not be provided for 33,3% of the targets to assess the reliability of the reported performance information. The municipality's records did not permit the application of alternative audit procedures

Additional matters

26. I draw attention to the following matters.

Achievement of planned targets

27. Refer to the annual performance report on pages x to x and x to x for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on usefulness and reliability of the reported performance information for the selected development priorities reported in paragraphs 19 to 25 of this report.

Compliance with legislation

28. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

29. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the integrated development plan (IDP), as required by section 41(1)(a) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and regulations 1 and 91(1)(a) of the Municipal Planning and Performance Management Regulations (MPPMR).

30. The performance management system and related controls were not in place as it did not describe and represent the processes of performance planning, monitoring, measurement, review, reporting, improvement and how it is conducted, organised and managed, including determining the roles of the different role-players, as required by section 38 of the MSA and regulation 7 of the MPPMR.

31. The annual performance agreements for the municipal manager and all senior managers are not linked to the measurable performance objectives approved with the budget and to the service delivery budget implementation plan, as required by section 53(1)(c)(iii) of the MFMA and section 57(1)(b) of the MSA.

32. The annual performance report for the year under review did not include measures taken to improve performance as required by section 46(1)(b) of the MSA.

Budgets

33. The total unforeseen and unavoidable expenditure incurred exceeded five percent of own revenue, in contravention of Municipal Budget and Reporting regulation 72.

Annual financial statements

34. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of receivables, revenue, commitment, irregular expenditure, budget statement, property, plant and equipment, accumulated surplus and cash flow identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided resulting in the financial statements receiving an unqualified audit opinion.

Procurement and contract management

35. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulations 17(a) and (c).

36. Contracts and quotations were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding and quotations, in contravention of SCM regulations 21(b) and 28(1)(a) and the Preferential Procurement regulations.

37. Contracts and quotations were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000).

38. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).

39. Sufficient appropriate audit evidence could not be obtained that all extension or modification to contracts were approved by a properly delegated official, as required by SCM regulation 5.

Expenditure management

40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.

41. Reasonable steps were not taken to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Conditional grants

42. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Infrastructure Grant allocation; Municipal Systems Improvement Grant allocation and Local Government Financial Management Grant allocation, as required by section 12(5) of DoRA.

Revenue management

43. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of the MFMA

Consequence management

44. Unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

45. The condonation of irregular expenditure was not approved by the appropriate relevant authority, as required by sections 1 and 170 of the MFMA.

46. Council certified unauthorised, irregular, fruitless and wasteful expenditure as irrecoverable without having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2)(a)(ii) of the MFMA.

Internal control

47. I considered internal control relevant to my audit of the financial statements, the annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

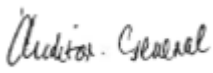
48. Leadership did not provide adequate oversight and monitoring controls in ensuring that effective measures were taken to address findings on the financial statements, as well as findings on predetermined objectives and compliance with legislation. This was due to a slow response in addressing the recommendations of the audit committee and internal audit.

Financial and performance management

49. Senior management did not implement proper record management systems for the maintenance of documents supporting reported financial and performance information. This contributed to the material findings on predetermined objectives and material adjustments that were required to the financial statements.

Governance

50. There was a lack of effective monitoring and evaluation by oversight structures over the financial and performance information in accordance with prescribed legislation and corporate governance principles.



Pietermaritzburg

27 November 2015